

STATE OF CALIFORNIA

Public Utilities Commission
San Francisco

M e m o r a n d u m

Date: March 15, 2016

To: The Commission
(Meeting of March 17, 2016)

From: Hazel Miranda, Director
Office of Governmental Affairs (OGA) – Sacramento

Subject: **AB 2168 (Williams) – Public Utilities Commission Audit Compliance Act of 2016.**
As introduced: February 17, 2016

RECOMMENDED POSITION: SUPPORT AS SPONSOR

SUMMARY OF BILL

AB 2168 codifies recommendations made by the State Auditor to the Legislature by amending Section 314.5 of the Public Utilities (PU) Code to make California Public Utilities Commission (CPUC) reports of inspections and audits and other pertinent information available on the CPUC's Internet Web site. At the same time, AB 2168 deletes the requirement that the CPUC furnish reports of its utility inspections and audits to the State Board of Equalization. The bill will also modify Section 792.5 of the Public Utilities Code requiring the CPUC to develop a risk-based approach to reviewing all balancing account periodically.

CURRENT LAW

- Section 314.5 provides that reports of inspections and audits and other pertinent information be furnished to the State Board of Equalization for use in the assessment of public utilities.
- Section 792.5 does not provide any guidance to the CPUC regarding its review of balancing accounts.

AUTHOR'S PURPOSE

AB 2168 codifies the State Auditor's recommendations to the Legislature regarding the Commission's review of utility balancing accounts and release of utility audit and inspection reports.

DIVISION ANALYSIS

Division of Water and Audits. AB 2168 will not impact the Division of Water and Audits' (DWA) current risk-based approach to reviewing amortization of balancing account balances as DWA is in compliance with the State Auditor's recommendations. DWA

risk-based approach in its review of water utility balancing accounts is to prioritize balancing accounts for review based on the impact that amortization of the outstanding balances will have on customer's utility bills. DWA reviews balances that exceed two percent of the annual Commission authorized revenue requirement, by which rates are set, for a utility or ratemaking district of a utility. For those balancing account balances that do not exceed the 2% threshold, the CPUC reviews and proposes adjustments to rates, either in the context of utility general rate case proceedings or regulatory audits performed pursuant to Public Utilities Code Section 314.5, to amortize under- or over-collections in any balancing accounts. DWA will be required to post reports of its inspections and audits of water and sewer utilities on the CPUC's Web site.

Energy Division. Since April 30, 2013, the CPUC's Energy Division requires utilities to file updated lists of balancing accounts and balances in each balancing account every quarter. The quarterly updates ensure that the CPUC will have timely information on utility balancing accounts.

Energy Division developed its risk based approach in August 2014 as part of the Balancing Account Review Procedures document. This document was provided to the State Auditor as part of the 6 month update in September 2014. The risk based criteria include the following:

1. Balancing accounts with quarter-end balances outside of $\pm 10\%$ or more of the currently authorized revenue requirement for a given account (ratio of balance to authorized revenue requirement).
2. Authorized revenue requirements that fall in the top 25th percentile of all accounts.
3. Volatile fluctuations in quarterly balances over time.
4. Accounts that have not been reviewed in the previous three reviews.

Balancing Accounts that meet the above identified risk-based criteria but are planned to be reviewed or audited by the Division of Ratepayer Advocates, the Division of Water and Audits, or by independent auditors are excluded.

Using the above risk based review approach, Energy Division selected 18 balancing accounts for in-depth review each year in 2014 and 2015. The reviews were done with the primary goal to ensure that the entries in the accounts were for allowable purposes and were supported by appropriate documentation (e.g. invoices and time cards when necessary). The risk based criteria will be revised based on our experience with the in-depth reviews. For each balancing account selected for in-depth review, staff reviewed and confirmed the utility's authorization to establish the account along with the pertinent information on the amounts authorized and the approved amortization. In addition to an examination of a sample of invoices, the review focused to verify that the allocation of overheads, the application of the franchise fee and uncollectibles (Franchise Fees & Uncollectibles – FF&U) factor and interest rate used were in accordance with the Commission's authorizing decisions. In performing the review at the invoice level, a

particular area of focus was transactions with affiliated companies to ensure ratepayers were not subsidizing affiliated businesses.

Since Energy Division has already been performing in-depth reviews of balancing accounts using a risk based approach per State Auditor's recommendations, there will be no impact on the Energy Division's current practice of balancing account reviews either.

SAFETY IMPACT

AB 2168 will neither reduce nor enhance the safety of California citizens.

RELIABILITY IMPACT

AB 2168 will neither reduce nor enhance reliability of service.

RATEPAYER IMPACT

Risk-based review of balancing accounts should benefit ratepayers. Putting the requirement in statute will help to guide the CPUC in the future. Paraphrasing the audit, rates are derived from projected costs and projected consumption of service, state law directs the CPUC to require utilities to establish balancing accounts to track the actual costs and the related revenues the utilities collect from ratepayers for certain activities. The purpose of a balancing account is to allow the utilities to recoup the costs the CPUC has authorized (in rate cases), while ensuring that ratepayers do not pay more than they should. Putting in statute a risk-based review of balancing accounts should help to enshrine risk-based review of balancing accounts. Risk based practices and benefit ratepayers in the long term. AB 2168 would not lead to increases in rates charged to consumers.

FISCAL IMPACT

AB 2168 will have not have a fiscal impact on the CPUC.

ECONOMIC IMPACT

AB 2168 would neither have a positive nor negative economic effect on businesses or the regulated community, including local government.

LEGAL IMPACT

No Legal impact.

LEGISLATIVE HISTORY

AB 825 (Rendon, 2015) would have deleted the requirement that the reports of the inspections and audit and other pertinent information be furnished to the State Board of Equalization for use in the assessment of the public utilities.

AB 2570 (Quirk, 2016) would delete the requirement that reports of the inspections and audits and other pertinent information be furnished to the State Board of Equalization.

PROGRAM BACKGROUND

AB 2168 is an outgrowth of the State Auditor's audit 2013-109 "California Public Utilities Commission: Improved Monitoring of Balancing Accounts Would Better Ensure That Utility Rates Are Fair and Reasonable." The audit noted that the CPUC lacks adequate processes to provide sufficient oversight of balancing accounts to protect ratepayers from unfair rate increases. The CPUC in the past relied on the Office of Ratepayer Advocates to review balancing accounts of energy utilities. The audit found the CPUC does not audit the accounting records of the utilities it regulates according to the schedule prescribed by law. This law codifies the State Auditor's recommendations into the Public Utilities Code. The intent of the law is to ensure that the CPUC regularly audits all utilities to increase public confidence in the regulatory process.

OTHER STATES' INFORMATION

None.

SUMMARY OF SUPPORTING ARGUMENTS FOR RECOMMENDATION

This bill should be supported for the following reason(s):

- (1) Requires CPUC reports of the inspections and audits of utilities to be made public by posting reports on the CPUC's web site.
- (2) Requires the development of a risk-based approach to prioritize the review of utility balancing accounts.

SUMMARY OF SUGGESTED AMENDMENTS

We are not suggesting any amendments to the changes made by this bill. However, given the changes to PU 792.5, it would be useful to take this opportunity to make a minor wording change. At present, PU 792.5(a) uses the term "reserve account" twice. It should be changed to "balancing account" because all decisions establishing these accounts use the term balancing account and not a reserve account. All utility filings seeking authorizations to amortize the balances in these accounts use the term balancing account.

STATUS

February 29, 2016 referred to Assembly Utilities & Commerce

SUPPORT/OPPOSITION

None on file.

VOTES

Not applicable.

STAFF CONTACTS:

Hazel Miranda, Director

Nick Zanjani, Senior Legislative Liaison

Michael Minkus, Senior Legislative Liaison

Lori Misicka, Legislative Liaison

Ivy Walker, Legislative Liaison

Hazel.Miranda@cpuc.ca.gov

Nick.Zanjani@cpuc.ca.gov

Michael.Minkus@cpuc.ca.gov

Lori.Misicka@cpuc.ca.gov

Ivy.Walker@cpuc.ca.gov

BILL LANGUAGE:

AB 2168 (Williams), as introduced February 17, 2016, Public Utilities Commission Audit Compliance Act of 2016.

http://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201520160AB2168